

The Highland Council

Pensions Committee and Pensions Board

22nd September 2016

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| Agenda Item | 4 |
| Report No | PC/04/16 |

Statement on Internal Control 2015/16 and Internal Audit Plan 2016/17

Report by the Audit & Risk Manager

Summary

The attached report includes an assessment of the adequacy, reliability and effectiveness of the Council's system of internal control and provides information for the Pension Fund's Annual Governance Statement contained within the 2015/16 Statement of Accounts.

In addition, details are provided of the audits being undertaken as part of the 2016/17 Audit Plan which Members are asked to approve.

1. Statement on Internal Control

- 1.1 In order to comply with the requirements of the Public Sector Internal Audit Standards, a Statement on Internal Control must be produced. Section 2 of the attached report gives details relating to the Statement on Internal Control and the sources of information which inform the Statement.
- 1.2 On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Pension Fund's internal control systems for the year to 31st March 2016.

2. Audit Plan 2016/17

- 2.1 A three year plan is in place for the Pension Fund which ensures that the main activities, which comprise of Pension Fund Investments, Contributions and Payments, are reviewed once every three years. The following work is being undertaken as part of the Pension Fund's 2016/17 Audit Plan:
 - (i) Audit Review of Pension Fund Contributions;
 - (ii) Work to support the Statement on Internal Control for 2015/16.

Both audits have been completed and copies of the final reports are attached as the next agenda item.

3. Implications

- 3.1 There are no Resource; Legal; Equalities; Climate Change/Carbon Clever; Risk and Gaelic and Rural implications arising from this report.

Recommendation

Members are invited to:

- (i) Consider the content of the attached report and the audit opinion provided, and to raise any relevant points with the Audit & Risk Manager.
- (ii) Note the status of this year's planned audits and to formally approve the 2016/17 Audit Plan.

Designation: Audit & Risk Manager

Date: 31st August 2016

Author: Donna Sutherland, Audit & Risk Manager

Background Papers



Highland Council Pension Fund
Statement on Internal Control 2015/16

1. INTRODUCTION

- 1.1 The purpose of this report is to provide an annual Internal Audit opinion for the period 1st April 2015 to 31st March 2016, and a report that can be used by the Pension Fund to inform its Annual Governance Statement.
- 1.2 This report has been produced in accordance with the requirements of the Public Sector Internal Audit Standards (the Standards) which came into effect from 1st April 2013 and apply to all internal audit service providers. These Standards were developed in collaboration between the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors (CIIA).
- 1.3 Section 2450 of the Standards states that *"the annual Internal Audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control. In addition, the annual report must incorporate:*
- *The opinion;*
 - *The summary of work that supports that opinion; and*
 - *A statement on conformance with the Standards and the results of the quality assurance and improvement programme."* As the Internal Audit service is provided by the Highland Council, this statement is provided within the Council's annual report.

2. STATEMENT ON INTERNAL CONTROL

2.1 Internal Control

Internal control is defined as *"the whole system of checks and controls, financial or otherwise, established by management in order to provide reasonable assurance"* regarding the achievement of one or more of the following objectives:

- The reliability and integrity of information.
- Compliance with policies, plans, procedures, laws, regulations and contracts.
- The safeguarding of assets.
- The economical and efficient use of resources.
- The accomplishment of established objectives and goals for operations or plans.

Any system of control can only provide reasonable, and not absolute assurance that control weaknesses or irregularities do not exist, or that there is no risk of material errors, losses, fraud or breaches of laws and regulations. Accordingly the Board should seek continual improvement in the effectiveness of its systems of internal control.

It is the responsibility of senior management to establish an appropriate and sound system of internal control, and to monitor the continuing effectiveness of that system.

2.2 Internal Audit

The Standards define internal auditing as *"an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes"*.

The work undertaken by Internal Audit is documented in an audit report and issued to management. Any areas of concern together with the management agreed actions and target dates for implementation are summarised in an Action Plan within the report. It is the responsibility of management to ensure that implementation of these actions takes place as agreed. The Internal Audit Section will undertake periodic follow-up reviews to ensure that the management agreed

actions have been satisfactorily implemented and the results of this will be reported to the Pensions Committee.

The Internal Audit Section operates in accordance with the Standards and as required, a risk based tactical audit plan is produced each year, and submitted for approval to the Pensions Committee.

2.3 Internal Audit work

The work undertaken by the Internal Audit Section during the year to 31st March 2016 consists of that undertaken directly for the Fund and indirectly where the Highland Council's financial systems are used. This consists of the following two audits:

- A review of the systems of internal control for the financial year 2015/16 consisting of a high level review of the adequacy and effectiveness of the Fund's system of internal control and targeted testing of key controls. These key controls, summarised below are examined to confirm that the main financial systems are operating as intended.
 - Financial procedures and guidance issued to staff;
 - Segregation of duties;
 - User access levels and appropriateness;
 - System backups.

No control issues have been identified from this work and the audit findings will be addressed in a separate report.

- An audit of Pension Fund Investments. Details of this audit were provided to the Pensions Committee on 24/09/15 including the audit opinion of "Full Assurance".

As part of the 2016/17 audit plan, a review of Pension Contributions has been undertaken which looked at transactions relating to 2015/16. No major control issues have been identified from the work undertaken.

Audit recommendations are action tracked to ensure that the management agreed actions have been satisfactorily implemented. A total of 3 audit recommendations were made during the year and all have been actioned as agreed as outlined below:

- In the Matters Arising from the Statement on Internal Control 2014/15, it was reported that the medium grade action to prepare a risk management strategy was still outstanding. This was completed and the strategy was presented to the Pensions Committee on 24/09/15.
- The Pension Fund Investments report contained 2 low grade recommendations both of which were implemented at the time. These related to the need to update process notes to show that any of the authorised bank signatories could authorise payments to the Custodian and to remove the unnecessary practice of undertaking month-end book cost reconciliations.

2.4 Assurances from Fund Managers and Global Custodian

The 7 Fund Managers and the Global Custodian each provide an annual assurance report (AAF 01/06/ISAE 3402) which sets out the control procedures in place during the year, and includes an assessment, by an independent accountant, of the effectiveness of the systems of internal controls in operation throughout the period examined.

These reports were obtained and reviewed, and it was confirmed that the appropriate assurances were provided by the independent accountants.

2.5 Governance arrangements

The Pension Fund has a Governance Policy Statement which is one of a number of key documents it must hold and this was last updated in May 2013. On 01/04/15

new governance arrangements came into place as a result of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015. As required, a Pension Board was established which holds joint meetings with the Pensions Committee.

The Highland Council, as administering authority of the Pension Fund, has approved and adopted a Local Code of Corporate Governance, which is consistent with the principles and reflects the requirements of the CIPFA/SOLACE Framework Note for Scottish Authorities – Delivering Good Governance in Local Government (2007). The Pension Fund arrangements comply with the CIPFA Statement.

2.6 Risk Management

CIPFA guidance on *“Managing risk in the Local Government Pension Scheme”* was issued in November 2012 and this sets out the role of the Pensions Committee as follows:

- Determining the risk policy and reconciling this with the wider organisational risk policy;
- Setting the risk management strategy in line with the risk policy;
- Overseeing the risk management process.

Within the Governance Policy Statement reference is made to the Fund’s Risk Management arrangements whereby identified risks and their countermeasures are contained within the Funding Strategy Statement (FSS). A new FSS was approved by the Pensions Committee on 19/02/15.

The Pension Fund has its own risk register which is based upon the format set out in the CIPFA guidance. Details of the risk management arrangements and an extract from the risk register were reported to the Pensions Committee on 14/08/15. As detailed at section 2.3, the Fund’s risk management policy and strategy was approved by the Committee on 24/09/15.

2.7 Audit Opinion

On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Pension Fund’s internal control systems for the year to 31st March 2016.